

TERMS AND CONDITIONS

For Licensed Activity of Electric Energy Distribution by ArmElNet Joint Stock Company

**(License No. 0092, issued in conformance with the ERC Resolution
No. 56A, dated August 30, 2002)**

1. Definitions used in the License

The following terms when used in this License shall have the meanings set forth below:

Generator - a legal entity that has been issued a License for the generation of electricity.

Exporter - a legal entity that has been issued a License for the export of electric energy from Armenia.

Electricity Distribution

Network or

Distribution

Network - a unified system of facilities (distribution lines, substations and other facilities) for the delivery of electricity from the Generator and (or) Transmitter to Consumers (Customers) and is operated and managed by the Licensee (Distributor).

Electricity Transmission

Network,

or Transmission

Network - a unified system of transmission lines, substations and other equipment that transmits electric energy from Generators or Importers to another Licensee and/or Consumer (Customer) and/or is transmitted to a third country, and is operated and managed by the Transmitter.

Legal Entity Having a

Right to Purchase

and Sell Electric

Energy - a legal entity that is issued an operations License, authorizing it to purchase and sell wholesale electric energy to other Licensees and/or Consumers (Customers).

Bilateral Electric Energy

Supply Agreement, or Bilateral

Agreement - an agreement between a Licensee and a Consumer (Customer) in need of electric energy, which specifies the terms and conditions for the supply and sale of electric energy.

Tripartite Electric Energy

Supply Agreement, or Tripartite

Agreement - an agreement among a Consumer (Customer), Sub-consumer (Sub-customer) in need of electric energy and a Licensee, that specifies the terms and conditions of electric energy supply and sales, the terms and conditions of operation and

maintenance used for supply of electric network electricity, which is not under the control of the Licensee, as well as the terms and conditions of compensation of the cost of the owner of that network

**Licensee, or
Distributor - Armenian Electric Network CJSC**

License - a document issued by the ERC to **Armenian Electric Network CJSC** which confirms the right and obligation of the above company to perform electric energy distribution services in the specified Service Area.

Transmitter - the legal entity that has been issued a License for the transmission of electricity via the Transmission Network.

Commission - the Energy Regulatory Commission of the Republic of Armenia, the regulatory body of the Energy sector.

Investments – investments agreed with the ERC, which result in an increase of used and useful Assets of the licensed operations.

Importer - a legal entity that has been issued a license to import electric energy into Armenia.

Tariff Margin - as defined in Chapter 1 of the Law of the Republic of Armenia on Privatization of Yerevan Distribution Closed Joint Stock Company, Northern Distribution Closed Joint Stock Company, Southern Distribution Closed Joint Stock Company, and Central Distribution Closed Joint Stock Company.

Consumer

(Customer) – a physical or legal entity, or an organization not holding a legal status in need of electric energy in the Service Area, that has signed a bilateral or tripartite electric energy supply contract with the Licensee.

Sub-consumer

(Sub-customer) - a physical or legal entity, or an organization not holding a legal status in need of electric energy in the Service Area, that has signed a bilateral or tripartite electric energy supply contract with the Licensee and will be using other Consumer's (Customer's) electric network for electric energy supply purposes.

Service Area – the geographic area shown in Appendix 1 to this license, in which in compliance with the License the Licensee is given the right to perform electric energy distribution service.

Confidential Licensee

Information – as defined in article 4 of the “Energy Law” of the Republic of Armenia.

Technological

losses – Sum of power unavoidable technical losses occurring in the distribution networks and determined on rated basis, and commercial losses that are due to errors in metering devices.

Force Majeure - causes or events that are beyond the reasonable control of, and without the fault or negligence of, the Licensee, including, but not limited to: unusually severe actions of the elements such as floods, earthquakes, hurricanes or tornadoes; sabotage; terrorism; war; riots or public disorders; strikes or other labor disputes;

to the extent such cause or event prevents or delays performance of any obligation imposed upon the Licensee claiming such force majeure event.

**Operator of Electric Energy
System or System**

Operator – Entity licensed by the Commission with functions defined in article 37 of the Energy Law of the Republic of Armenia.

Rules of Electric Energy Market

or Market Rules – As defined in article 4 of the Energy Law of the Republic of Armenia.

Distribution Service

Tariffs – Service Tariffs of the Licensee for distribution of electric energy of other entities via Distribution Networks to Consumers (Customers), Service Tariffs of other Licensees having the right to distribute electric energy in the Republic of Armenia, and/or Service Tariffs to transmit electric energy to third countries, all of which are stated by the ERC based on the principle of necessary profit requirements of the Licensee.

**Rules of Supply and Use of
Electric Energy or Rules of Supply**

and Use – ERC-approved regulations which state the rules of electric energy supply from the Licensee to Consumers (Customers) as well as the rules and conditions of electric energy use by the latter.

2. Effective Period of the License

2.1 This License is issued for an unlimited period of time, with the limitation of some exclusive rights of the Licensee as stated in article 3.3 of the License.

3. Essential functions of the Licensed Activity

3.1 On and after the Effective Date, the Licensee has a right and is obliged to perform the following essential functions of electricity distribution within the Service Area:

- a) Maintenance, operation and improvement of the Electric Distribution Network;
- b) Supply of electricity to Consumers (Customers) via the Electric Distribution Network;
- c) Expansion of the Electricity Distribution Network and connection of new consumers with the purpose of satisfying the need for electric energy in the Service Area;
- d) Wholesale purchase of electricity from Licensees that have the Right to Purchase and Sell Electric Energy for the purpose of supply of the electric energy to the Consumers (Customers);
- e) Sale of electricity to Consumers (Customers);
- f) Installation and maintenance of commercial meters, including those at the premises of Consumers (Customers);
- g) Management and dispatch of the Distribution Network;
- h) Signing Bilateral and Tripartite electricity supply Contracts, and collection of payments for electric energy supplied (sold).

- 3.2 The Licensee is given the exclusive right to carry out the functions specified in points a), b), c), e), f), g) of article 3.1 of the License within the Service Area, except in the cases specified in Item 2 of Article 47 of the Energy Law.
- 3.3 The Licensee is given the exclusive right to carry out the functions specified in points d) and h) of article 3.1 of the License for the period stated in Sub-Item b) of Item 1 in article 59 of the RoA Energy Law, except the cases specified in Item 2 of Article 47 of the Energy Law.
- 3.4. For the purpose of ensuring the direct connection of other Consumers' (Customers') electric installations and/or power lines to the distribution network in the service area, the Licensee has the right to implement investment plans for that purpose. The Commission shall evaluate the reasonableness and economic efficiency of the plan, and if it approves the plan, its measures shall be implemented and coordinated with the Commission, and the justified and necessary expenses shall be included in the Tariff Margin and/or in the Distribution Service Tariffs. The Licensee may file the plan described in this article separately, or as part of the investment plan described in article 4.9 of this license.
- 3.5 The Licensee has no right to assign, hypothecate, transfer, yield or give the rights or obligations bestowed by this License (by contract or otherwise, partially or completely) to any other entity or entities, without the prior consent of the Commission.
- 3.6 For the purposes of performing its licensed activities and preventing losses, the Licensee shall have the right of free access to substations, which are not owned by him and which feed Consumers (Customers) and/or Licensee, to control and to implement effective and reasonable technical measures, in accordance with Market Rules provisions and/or model contracts or mandatory conditions approved by the Commission.

4. Provision of Licensed Activity

- 4.1 The Licensee shall perform all Licensed Activities in conformance with the laws of the Republic of Armenia, including the Energy Law, the Law on Privatization of Yerevan DC CJSC, Northern DC CJSC, Southern DC CJSC and Central DC CJSC, the License, as well as requirements of Legal Acts established by the Commission, and other legal acts.
- 4.2 As provided in point 1 of article 38 of the Energy Law, when the License is enacted the Licensee has the right and is obligated to distribute electric energy to Customers (Consumers) connected to its network in its service area, as well as to suggest to new customers, or those who are in reconstruction, the technical conditions for connection to the distribution network or to other Customers' (Consumers') electric installations to ensure service of electric energy to them.
- 4.3 The Licensee, within the limits of its technical capability shall transmit electrical energy owned or possessed by other entities with Distribution Service Tariffs of the ERC through the Distribution Network to border points, in accordance with article 53 of the Energy Law and the Market Rules.
- 4.4 After the completion of the term stated in point 1-b) of article 59 of the Energy Law, the Licensee, within the limits of its technical capability, shall be required to provide open access to other entities having the right to purchase and sell electric energy to its Distribution Network, as well as to provide distribution of electric energy to Consumers (Customers), at Distribution Service Tariffs set by the Commission in accordance with

Article 53 of the Energy Law and the Market Rules.

- 4.5 The Licensee shall ensure service and maintenance, including testing, of all commercial metering devices used to supply power to Consumers (Customers).
- 4.6 The contracts signed between the Licensee and other entities having a License for operation in the electric energy sector shall comply with the conditions of model contracts and/or mandatory conditions established by ERC. Those contracts shall be effective from the moment of their registration at ERC.
- 4.7 The Licensee shall carry out the orders and instructions of the System Operator in compliance with the Market Rules, the acting technical regulations of the Republic of Armenia, and the provisions of service agreements.
- 4.8 In compliance with the Market Rules, technical regulations of the Republic of Armenia, and provisions of service agreements, the Licensee shall be required to support the System Operator's inspection of the Licensee's protective devices and regulators that ensure the safety and reliability of the electric energy system, provide the operation of such devices in conformance with the Republic of Armenia's Legislation and other legal acts and documents, carry out repair, replacement and other essential operations, and support the inspection of protective devices and regulators under his control yet owned by other entities.
- 4.9 Within 5 months starting the day the License comes into effect, the Licensee should submit for the approval of the Commission the plans on improvement and expansion of the Distribution Network, on bringing its licensed activities into correspondence with the technical rules, as well as on improvement of quality of the service provided to the Customers (Consumers) and environment protection investment plans, all containing correspondent justifications. The initial plan of the Licensee should contain investment suggestions for the first year. On the basis of submitted plans, including the necessity and effectiveness of the investments, the analysis of their impact on the future tariff margin and (or) the distribution service tariffs, the Commission should whether completely accept the plan or completely reject it, or approve it partially, within 60 days. The Licensee shall accomplish the investment plan coordinated with the Commission, and the investments implemented in accordance with the plan shall be included into the tariff margin and (or) the distribution service tariff, according to the methodology introduced in Appendix 2 of this License.

Six months later after the approval of the investment plan and, further on, each year the Licensee shall introduce the investment plan for the next three years. The Commission shall review it and issue a resolution, in consistence with the established procedure.

In case, if the Licensee implements an investment plan, which was rejected by the Commission in defined procedures, then the improved indicators resulted from the implementation of the plan will not be considered by the Commission while setting tariffs until the Licensee returns back the investments. If the Licensee decided to implement the rejected investments plan at its own risk, it must keep the Commission informed and conduct a separate accounting for that plan.

- 4.10 Within 12 months after the commencement of the License, the Licensee shall submit to the Commission the methodologies of calculation of Technological Losses. In case of disputable issues regarding the plan, it should be forwarded for testing to the jointly selected experimental company or to individual experts. The disputable issues regarding the value of

Technological Losses included into the Tariff Margin and Distribution Service Tariffs of the Licensee, shall also be solved on that principle.

- 4.11 In compliance with the procedure and within a timeframe established by the ERC, the Licensee shall present to the ERC the forecasted load profile, consumption volume and Technological Losses for the next year.
- 4.12 The Licensee shall present to the ERC information and reports about its licensed activity in procedures and forms established by the Commission.
- 4.13 The accounting and reporting of the licensed activity shall comply with the accounting requirements set forth by the Republic of Armenia Legislation and in compliance with requirements of legal acts of the ERC.
- 4.14 The Licensee shall be required to keep separate accounting for the licensed activity.
- 4.15 By May 30 of each year the Licensee shall publish financial statements of its previous year's activity printed in Armenia in compliance with the forms established by the Commission.
- 4.16 Information submitted to the ERC is available to the public unless it is designated as confidential by the Licensee and marked as "confidential information of the company". The Licensee shall, in such a case; state in writing how the publication of the information (including "confidential information of the company") can harm the competitiveness of the company and that its interest has a higher priority than the public. The Commission may accept or deny the Licensee's request.
- 4.17 The Licensee's acquisitions of equipment and service shall take into consideration the requirements of Article 9 of the Law on Privatization of Yerevan DC CJSC, Northern DC CJSC, Southern DC CJSC and Central DC CJSC.
- 4.18 The Licensee must make all purchases, including procurement of services and commodities in compliance with the procedure on making purchases, which shall be confirmed by the Commission in the presence of the Licensee. The Licensee shall forward the above procedure for the Commission approval within the period of 3 months after the License commencement date.
- 4.19 The Licensee shall be held responsible for the accuracy of the reports on licensed activity and any other information presented to the Commission.
- 4.20 Starting the License commencement date and up to January 1, 2004 the fixed Tariff Margin expressed in US currency will be effective for the Licensee and will amount to 1,59 US cents/ kWh equivalent drams, before VAT. Beginning January 1, 2004 the Tariff Margin will be calculated by the methodologies defined in Appendix 2 of this License, however it should not be less than the amount in drams equivalent to 1,50 US cents/kWh, before VAT.
- 4.21 The justified damages and (or) supplementary expenses of the Licensee conditioned by amendments to the RoA Legislation, effective legal acts, technical rules and standards or approval of new ones, shall be compensated through the Tariff Margin and (or) the Distribution Service Tariffs. In case of disputes with the Licensee in relation to the amounts

of supplementary expenses or damages subject to compensation, the Commission, in cooperation with the Licensee, shall involve the independent experts.

- 4.22 Within the timeframe endorsed in the Electric Energy Sale/Purchase Agreements, the Licensee shall be required to make 100% payments for electric energy purchased, services provided to him, and works performed.
- 4.23 The Licensee shall be required to implement programs for compliance with the requirements of safety and environmental norms of the Republic of Armenia within the framework and timetable approved by ERC. During the implementation of the approved program, any deviations from the requirements of the norms and standards set forth in the technical rules and procedures of such program shall not be considered breach of those norms. The Licensee shall submit the above-mentioned programs to ERC within 12 months from the effective date of the License.
- 4.24 The Licensee shall inform the ERC immediately about any circumstances that have resulted in or may lead to any violation of the provisions of the License.
- 4.25 The Licensee shall ensure reliable electric energy supply to the Consumers (Customers) according to the requirements of article 4.28 of the License.
- 4.26 The relations between the Consumers (Customers) and the Licensee shall be regulated by the Supply Contracts, the model forms of which shall be established by the ERC, Rules for Electric Energy Supply and Use, laws and other legal acts.
- 4.27 The Licensee shall implement disconnections of the Customer (Consumer) caused by renovations and for non-payment, as well as restoration of the electric energy supply after any disconnections, in compliance with the procedures stated in the contract and in the Rules for Electric Energy Supply and Use.
- 4.28 The ERC shall evaluate the quality of the service provided by the Licensee to the Customers (Consumer) annually based on the analysis and comparison of the following Licensee's indicators and those of other countries deemed appropriate for benchmarking.
- a) The average interruption frequency grouped per reasons of interruptions experienced by all customers as determined by the overall number of customer interruptions in a year divided by the average number of customers served during that year,
 - b) The average interruption duration experienced by all customers as determined by the overall number of customer interruptions in a year in minutes divided by the average number of customers served during that year,
 - c) Overall number of Customers complaints distinguished by reasons and customer groups,
 - d) The number and duration of voltage and frequency deviations from the allowed frames as determined by an approved sampling of the system.

While calculating the above indicators, disconnections and decrease of customer service quality resulting from Force Majeure events shall not be included, nor shall service problems caused by the activity or facilities not owned or managed by the Licensee. The Licensee shall submit special report on such events to the ERC.

4.29 Within the maximum 18 months after the commencement of the License the Licensee shall submit to the Commission the report of the previous 12 months on the actual values of indicators mentioned in point 4.28 of this License, as well as the plans of necessary measures targeted the improvement of those indicators, including the long-term and short-term investment plans. The Commission shall issue a resolution on the introduced plans, according to point 4.9. of this License, and the projected values by years defined in point 4.28 of this License shall be approved by the Commission resolution.

4.30 The Licensee shall be required to have 24-hour telephone communication in its service regional offices, which shall enable the Customers (Consumers) to inform or receive information.

4.31 The Licensee shall install commercial night-time tariff meters, which can record night-time consumption of electric energy and are purchased (bought) by the Consumers (Customers, including the population), which shall comply with requirements of the technical norms and procedures of the Republic of Armenia and conditions coordinated with the Commission.

Before the effective day of the License, the advance payments of customers associated with purchase of such kind of meters, are subject to compensation, according to the RoA "Law on Privatization of the "Yerevan Disco", "Northern Disco", "Southern Disco" and "Central Disco" Closed Joint-Stock Companies" and the procedure established by the Commission.

4.32 The Licensee may disconnect the supply of electricity to a Consumer (Customer) if the Consumer (Customer) does not pay a bill within the period of time established by the electric energy supply contracts. Such disconnection from the electric energy supply shall follow all warning procedures set forth by the Commission. The Licensee shall have the right to impose and levy penalties on Customers (Consumers), except for Residential Customers (population), in compliance with procedures and in amounts provided by Supply Contract and Rules for Electric Energy Supply and Use. According to the Rules for Electric Energy Supply and Use, legal acts of the ERC, and the Legislation of the Republic of Armenia, the Licensee is obligated to supply the VIP Consumers (Customers) based on article 11 of chapter 2 of the Privatization Law for Yerevan DC CJSC, Northern DC CJSC, Southern DC CJSC and Central DC CJSC.

4.33 The Licensee cannot possess 25% or more of the shares of another Licensee, or merge with another Licensee without ERC permission. The Licensee should apply to the ERC for the approval of sales or transfer of ownership of company's fixed assets, which are necessary for the licensed activity (buildings, constructions, production forces, acting electric installations and power lines). The Commission makes appropriate decision within 60 days in case of approval of application under some basis mentioned in this item.

4.34 In performing licensed activities, the Licensee shall protect the life and health safety of population and service personnel according to the Legislation of RoA.

4.35 The Commission must mention reasons for refusal in the application, in case of making negative decision on the application represented by the Licensee. In the event the Commission does not reply to the application of the Licensee within the timeframe mentioned in this License or orders defined by the Commission, the application considers shall be acceptable. In the event there is no time for reply to the application represented by the Licensee specified in this License or orders defined by the Commission, such time is considered shall be 60 days.

- 4.36 Management staff of the Licensee shall comply with the criteria prior coordinated with the Commission by the Licensee.
- 4.37 The Licensee has no right to be involved in another economic activity without agreement of the Commission.
- 4.38 The Licensee can open bank accounts, transfer or make analogical changes only upon agreement of the Commission.
- 4.39 To ensure the guaranteed payments to the generating companies and service providing companies for the delivered energy (capacity) and rendered services, the Licensee shall open a special bank account in an Armenian commercial bank. The amounts entered to that account in the beginning of each month are considered collateral in favor of the power (capacity) generating companies and service providing companies, as a measure to guarantee the payment of debts accumulated by the end of the previous month. The collateral will be terminated after the payment of liabilities accumulated by the end of the previous month.
- 4.40 The Licensee must enter the cash amounts collected from or transferred by the consumers for the distributed electric energy into the special account, specified in point 4.39.
- 4.41 To ensure the guaranteed payments to the generating and services providing companies for delivered power (capacity) and rendered services the Licensee shall pledge a guaranteed sum with the same bank agreed with the Commission, and the sum is considered an additional measure to guarantee payment of debts accumulated by the end of the previous month. In case of complete or partial use of that sum, the Licensee must supplement the defined size of money within a 3-day period. The guaranteed amount for the year 2003 makes 600 000 US dollars, and starting 2004, the amount will be 10 % of the total amount received for services rendered and power (capacity) sold during each month of the previous year in average.
- 4.42 The Commission in cooperation with the market participants shall establish the procedure on making payments from the special accounts and using the guaranteed amounts. Upon the approval of the mentioned procedure, the Licensee must introduce orders on enforcement of that procedure to the bank serving the special account, specified in point 4.39 and the guaranteed payments account specified in point 4.41.

5. Supervision of the Licensed Activity

- 5.1 The ERC shall supervise Licensee's compliance with the provisions of this License in accordance with the RoA legislation and procedures set by the ERC.
- 5.2 In order to ensure compliance with the License provisions, the ERC and its authorized representatives shall have the right of free access to the premises of the Licensee. In the course of such inspections, the Licensee shall fully cooperate with and render assistance to the ERC and its authorized representatives.
- 5.3 In the Licensee's territory the authorized representatives of the ERC shall comply with the internal procedures of the company, safety and firefighting rules, as well as norms set by the RoA Legislation.

5.4 The ERC, with prior notification to the Licensee, shall perform a study of Licensee's compliance with the provisions of the License, check the accuracy of the reports presented to the ERC using procedures and within a timeframe set by the RoA legislation and by itself, but not more than once per year and with the help of an independent expert company or independent experts selected by itself. The expenses for such studies and inspections shall be included in the Tariff Margin and (or) Distribution Service Tariff. Such expenses may not be fully or partially reimbursed through Tariff Margin and (or) Distribution Service Tariffs, if as a result of such inspection or study the Commission finds that the Licensee has intentionally presented fraudulent data to ERC or concealed any data from ERC.

6. Penalties, License Suspension and Revocation

6.1 In the event of non-compliance, inappropriate compliance or violation of the Energy Law, requirements of legal acts of ERC and License provisions, the ERC is authorized to impose the following penalties, in accordance with Article 42 of the Energy Law.

- a) Warning and assignment to eliminate the violation
- b) Decreasing of Tariffs
- c) Licence suspension
- d) Licence révocation.

The procedures for enforcement of the above penalties are determined by the ERC in accordance with Article 42 of the Energy Law.

6.2 In the event of License revocation, Article 52 of the Energy Law and Republic of Armenia Legislation shall guide the ERC and the Licensee.

6.3 The License may be terminated at the initiative of the Licensee, after a notice in writing. In such a case, the ERC and the Licensee shall be governed by Article 52 of the Energy Law and the Legislation of the Republic of Armenia. The Licensee shall continue the licensed operation in compliance with the License provisions until the issuance of a corresponding decision on termination by the ERC.

6.4 The Licensee shall not be liable under procedure defined by item 6.1 of this License if (to the extent) license violations were caused by Force Majeure circumstances

7. Amendments to the Terms and Conditions of the License

7.1 The review and approval of Licensee's applications to modify the License shall be conducted in accordance with procedures established by the Commission.

The License provisions may be modified based on the initiative of the Commission, only with the consent of the Licensee, unless the intended amendments are required for adequate implementation of the Republic of Armenia's laws.

Additional expenses incurred by the Licensee, resulting from the modification of License provisions initiated by the Commission, shall be included into the Tariff Margin and/or Distribution Service Tariffs.

8. Notification

- (i) **8.1 All official notifications, applications (petitions), claims or other correspondence associated with this License shall be in writing and be**

delivered via messenger or registered mail, requiring a verification of return receipt. All notices or other correspondence shall be considered effective only upon actual delivery or receipt, or, if the notice did not reach the addressee due to the addressee's fault, upon the moment of presenting. The message may be delivered by e-mail or fax and shall become effective from the moment of receipt, if it has been received by the end of the given business day.

APPENDIX 1
Of the License Terms and Conditions approved by the RoA
ERC Resolution No 79A, dated November 1, 2002

GEOGRAPHIC AREA OF THE LICENSED ACTIVITY

GEOGRAPHIC AREA OF ELECTRICITY DISTRIBUTION ACTIVITY

1. Territory of the Republic of Armenia

Methodology of Tariff Margin Calculation

1. Tariff margin for Licensee will be calculated in accordance with the methodology based on the principle of the revenue requirement of the Licensee, i.e.

Revenue Requirement = Operation & Maintenance Expenses + Depreciation +
Cost of Purchased Electric Energy + Taxes + Bad Debts + Allowed Net Profit
(After Taxes)

where:

Operation and Maintenance Expenses will include the cost of technical service and repair, necessary materials for operation, salary, mandatory social insurance payments, administrative, management, sale and other general costs allowed by the Commission.

Until January 1, 2004, the annual operation and maintenance expenses included in Tariff Margin calculation will be equal to 28 mln. USD. Further on they will be defined based on analysis of actual expenses taken from financial statements and from summaries of independent experts.

Depreciation will be calculated by straight-line method. The depreciation of fixed assets at the moment of privatization will be calculated based on 100 % of shares issued after the tender and according to the share purchase agreement, the value of liabilities transferred to the Licensee. The depreciation rate of those assets will be 10 %:

The depreciation rate of assets generated from further investments will be 4 %.

Cost of both initial assets and those created due to investments made in the process will be fixed in Armenian drams. Expenses that will incur in foreign currency will be reevaluated in equivalent Armenian drams using current exchange rate. Those assets should be re-evaluated only in USD/AMD exchange composition and only if after the last re-evaluation the change is more than 3%.

Cost of Purchased Electric Energy will be calculated by the following formula:

Cost of Purchased Electric Energy = [Electric Energy Sold in kWh: (1- losses rate allowed by the Commission)] x Weighted average tariff of purchased Electric Energy.

Taxes (except the VAT) will be calculated in conformance with the Tax Legislation of RA, based on the revenue and costs included in Tariff Margin calculations.

Bad Debts, which represent the cost of electricity delivered by the Licensee to the Consumers (Customers) but not paid for, will be included in the Revenue Requirement, but no more than 2% of cost of supplied electric energy.

Allowed Net Profit will be determined by the following formula:

Allowed Net Profit = Profit Rate Base x Rate of Return on Assets

Profit Rate Base will be determined based on 100% of shares generated in the process of tender plus the liabilities transferred to the new company according to share purchase agreement plus accumulated investments in used and useful assets (fixed and current) made from the closing date until the date of the revision of Tariff Margin minus accumulated depreciation. The Profit Rate Base will not include those investments, which are obtained in the form of grants or favorable loan received from or through the mediation of the Armenian Government. The service cost of such loans are included in the operation and maintenance costs Expenses Working capital size, which will be included in profit rate base, will be calculated as the difference between current assets and current liabilities necessary for the licensed operation, which will be defined based on the turnover period approved by ERC. Cash required for credit repayments will not be taken into account.

Tariff Margin will be determined by the following formula:

Tariff Margin = (Revenue Requirement: Electric Energy Sold in kWh) - Weighted average tariff of purchased electric energy.

- 1.1 In each calendar year until 2009 the Commission will provide a 17% Rate of Return on Assets applied to the Profit Rate Base. Starting from 2010 the Commission, via the analysis of the other industrial companies' profitability operating in Armenia under the same risk level, will determine such Rate of Return on Assets not less than 12%.
- 1.2 In case the Commission changes the tariffs for electricity purchased by the Licensee, both the retail tariffs for electricity sold to Consumers (Customers) and the part of distribution companies Tariff Margin related to the cost of losses considered allowable by the Commission, will be correspondingly changed.
- 1.3 Allowed losses of electric energy that will be included in Tariff Margin calculations will make up 17% of purchased power for year 2004, 15% for 2005, and 14% for 2006, 13,5% for 2007, and 13% for 2008. For the next years the volume of allowed losses that will be included in the Tariff Margin calculation will be in accordance with article 4.10 of the License and in compliance with the methodology of technological loss estimation. Estimated yearly losses in accordance with article 4.10 of the License, as a sum of technical losses and commercial losses due to metering device errors will be included in the calculations of Tariff Margin. Other commercial losses will be included in the tariff margin after analysis of results of financial statements of licensed activity, or programs aimed at losses minimization including investment programs, but in any case it will be included in tariff margin calculation with not less than 1% rate of purchased power and not more than the difference between previous year actual losses and estimated technological losses.
- 1.4 Tariffs are calculated at Armenian dram and US dollars average exchange rates for appropriate period accepted as the base of the State Budget of RA and are stated in Armenian drams. If according to official information of The Central Bank of RA,

the actual average exchange rate deviates from the exchange rate used to calculate the current tariff more than by 3%, the tariffs and tariff margin may be amended but no more often than semiannually.

In 2002-2003 an adjustment to the tariff margin expressed in Drams shall be made so, that an annual average weighted rate of the tariff margin remains within the average weighted margin stated in article 4.20 of the License.

Starting from year 2004 changes in exchange rate shall cause adjustments only at the part of expenditures, which were made in foreign currency and are related to profit and depreciation. Changes in expenditures made in Armenian Drams and resulting from changes in prices in the domestic market shall be taken into account in compliance with procedures of tariff revision.